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June 1, 2004

CALIFORNIA OVERNIGHT

Gerardo C. Rios
CHIEF, PERMITS OFFICE, AIR DIVISION
U.S. ENVIRONMENTAL PROTECTION AGENCY
75 Hawthorne Street
San Francisco, CA 94105

Re: **BHP Billiton – Cabrillo Port Project**

Dear Mr. Rios:

On behalf of our client, BHP Billiton LNG International Inc. (BHPB), this is in response to the preliminary conclusions reached in EPA's letter of April 5, 2004.

BACKGROUND

BHPB proposes to construct "Cabrillo Port," an offshore liquefied natural gas importation terminal, in compliance with the Deepwater Port Act, 33 USC §§ 1501, *et seq.* (DPA). Cabrillo Port consists of a floating storage and regasification unit (FSRU) connected to a new subsea pipeline that will come ashore at Ormond Beach, near Oxnard, where the pipeline will connect to existing onshore natural gas transmission systems operated by Southern California Gas Company. The FSRU will be located approximately 14 statute miles offshore Ventura County.

The FSRU is to be a ship-shaped, double-sided, double-bottom LNG storage and regasification vessel approximately 283 meters long and 65 meters wide. The FSRU will be moored to the seabed in federal waters by a fixed, turret-style mooring point. The FSRU is properly characterized as a "natural gas transmission" facility (SIC Code 4922). The ships that transport LNG to the FSRU, the tugs that assist these cargo

vessels, and the crew and supply boats that ferry personnel and supplies to the FSRU are properly characterized as "water transportation" (SIC Code 44).[1]

Pursuant to the DPA, Cabrillo Port is a "new source" as defined by the federal Clean Air Act (CAA). Because the FSRU will be situated in an offshore area that has not been designated as "non-attainment" (40 CFR § 81.305), BHPB submitted an application for a PSD permit (40 CFR §§ 52.21, *et seq.*) to EPA Region IX on January 19, 2004. A PSD area is one designated pursuant to CAA § 107 and 40 CFR Part 81 as either "attainment" or "unclassifiable" for a criteria pollutant. See, USEPA, "New Source Review Workshop Manual, PSD and Nonattainment Area Permitting", p. A.1.

In its April 5 letter EPA preliminarily concluded, among other things, that the agency intends to apply the air rules for facilities governed by the Outer Continental Shelf Lands Act (OCSLA), and that the offset requirements of Ventura County APCD Rule 26 would be applied to BHPB's permit application. We appreciate the opportunity to consider EPA's initial analysis. However, as explained below, the CAA rules for Outer Continental Shelf (OCS) facilities do not apply to Cabrillo Port, and EPA should not and cannot import into the DPA licensing process a series of requirements that Congress has declined to apply to deepwater ports. Cabrillo Port should not be treated as if it were located in a non-attainment area and a PSD permit is appropriate for the facility. Moreover, the DPA does not require or permit the attribution to Cabrillo Port of emissions from marine vessels when those vessels are in transit to or from the port, or when such vessels are "hotelling". [2]

LEGAL ANALYSIS

A. Points of Agreement and Disagreement Between BHPB and EPA.

There appear to be several key points upon which BHPB and EPA agree:

1. Both parties agree that Cabrillo Port is a "deepwater port" governed by the DPA;

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[1] In view of the conclusions reached here we do not discuss, although BHPB preserves the right to raise, international law issues applicable to vessels on the high seas.

[2] While docked at port, ocean-going cargo vessels shut off their propulsion engines and use auxiliary diesel generators (internal combustion engines) to power refrigeration, lights, pumps, and other functions. These activities are commonly called "hotelling".

2. Both parties agree that, as a deepwater port, Cabrillo Port is to be considered a "new source" under the CAA and must secure preconstruction and operating permits from EPA; and

3. Both parties agree that Cabrillo Port is not an "Outer Continental Shelf source" as defined in CAA section 328, and that Cabrillo Port is not governed by the regulations promulgated under section 328.

There are also key points upon which BHPB and EPA seem to disagree and merit further discussion. We address these points in more detail below. In brief, they are:

1. EPA's preliminary conclusion that the CAA rules for Outer Continental Shelf sources should be applied to this deepwater port; and

2. EPA's apparent preliminary conclusion that the DPA permits attribution to Cabrillo Port of the emissions from marine vessels in transit to and from the deepwater port.

We disagree that while the OCS air regulations do not apply to deepwater ports, the application of these regulations to this deepwater port project is nonetheless appropriate. Moreover, we do not believe EPA has authority to require Title I preconstruction review or Title V operating permits with respect to marine vessels calling at the port.

B. The Structure of the DPA and EPA's Role in the Licensing Process for Deepwater Ports, Which Exclude Marine Vessels.

Congress enacted the DPA in 1974 to regulate the construction and operation of deepwater ports. Congress passed the Deepwater Port Modernization Act in 1996, and the Maritime Transportation Security Act in 2002, the latter of which extended the definition of "deepwater port" to include LNG facilities. Temporary Interim Rules governing the licensing and operation of deepwater ports are found at 33 CFR Parts 148, 149 and 150 (69 Fed. Reg. 724, January 6, 2004).

Unlike OCS platforms and other facilities associated with the multi-faceted operations involved in exploration and production of mineral resources of the OCS, deepwater ports are in essence single-purpose transportation hubs. Unlike OCS facilities, which are subject to regulation by the Minerals Management Service on behalf

of the Department of the Interior (DOI), Congress provided that deepwater ports are subject to regulation by the Department of Transportation, which in turn has delegated authority over such deepwater ports to the U.S. Coast Guard and the Maritime Administration (MARAD).[3]

EPA's role in deepwater port licensing stems from section 1502(9) of the DPA, which provides that "[a] deepwater port shall be considered a 'new source' for purposes of the [CAA and the CWA]. . . ." One of the conditions precedent to obtaining a license for such a deepwater port is that:

> [The Secretary of Transportation] has not been informed, within 45 days of the last public hearing on a proposed license for a designated application area, by the Administrator of the Environmental Protection Agency that **the deepwater port** will not conform with **all applicable provisions** of the Clean Air Act, as amended [42 USCS §§ 7401 *et seq.*], the Federal Water Pollution Control Act, as amended, or the Marine Protection, Research and Sanctuaries Act, as amended . . . ." 33 USC § 1503(c)(6); emphasis added.

The DPA defines a "deepwater port" as "any fixed or floating manmade structures ***other than a vessel,*** or any group of structures, that are located beyond State seaward boundaries and that are used or intended for use as a port or terminal for the transportation, storage, and further handling of oil or natural gas for transportation to any State. . . ." 33 USC § 1502(9)(A); emphasis added. Vessels, which are expressly excluded from the definition of "deepwater port," are broadly defined in the DPA as "every description of watercraft or other artificial contrivance used as a means of transportation on or through the water." 33 USC § 1502(19).[4]

Thus, in providing that a deepwater port will be considered a "new source" for purposes of the CAA, Congress has expressly excluded vessels from the types of facilities that can constitute a "deepwater port." It is apparent from the structure of the DPA that Congress intended to limit the scope of EPA's CAA review process to the

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[3] The Coast Guard is in the process of transitioning from DOT to the new Department of Homeland Security (DHS).

[4] A "natural gas deepwater port" is also defined in the DPA, adding further emphasis to the fact that marine vessels are not included among a deep water port's components. The definition includes "all components and equipment, including pipelines, pumping or compressor stations, service platforms, buoys, mooring lines, and similar facilities that are proposed or approved for construction and operation as part of a deepwater port . . . ." 33 USC §1502(9)(C).

deepwater port itself. This necessarily excludes any vessels involved in transporting cargo, supplies or personnel to or from deepwater port facilities. See, e.g., *Santa Barbara County APCD v. USEPA*, (D.C. Cir., 1994) 32 F.3d 1179, 1181 ("[W]e find it was reasonable for the EPA to conclude that OCS sources did not include vessels that were merely traveling over the OCS.") Federal regulatory authority over a deep water port does not extend beyond that authorized by the DPA. See, e.g., S. Rep. No. 93-1217; 1974 USCCAN 7529, 7536. Consequently, marine vessels are not properly considered part of the "new source" for purposes of EPA's Title I preconstruction review or Title V operating permits in assessing the deepwater port's compliance with the CAA pursuant to DPA 33 USC § 1503(c)(6).

C. The OCS Air Regulations Do Not Apply.

EPA's April 5 letter suggests that regulations applicable to OCS facilities, in particular those attributing to an OCS source the emissions from vessels serving or associated with the OCS source, may be imported into the DPA. We disagree. EPA's preliminary view runs counter to the plain language of the DPA and to the history of Congressional legislation on the subject of offshore facilities.

In 1990, Congress assigned to EPA responsibility for controlling air pollution produced in the OCS by adding section 328 to the CAA. 42 USC § 7626. Subsection (a)(1) of section 328 requires the Administrator to establish requirements to control air pollution from OCS sources. Section 328 also requires attribution to the OCS source of vessel emissions within 25 miles of the OCS source. The Ventura County APCD rules dealing with OCS emission sources derive from EPA's delegation of authority to the local district pursuant to section 328. 42 USC § 7627(a)(3).

Congress has not made the provisions of section 328 applicable to "deepwater ports." Instead, Congress expressly limited the scope of section 328 to "OCS sources", facilities that do not include deep water ports. 40 CFR §§ 55.2 & 55.3. An "OCS source" is one engaged in the exploration, development or production of minerals of the Outer Continental Shelf. 43 USC §§ 1331, *et. seq.* Moreover, the term includes "vessels" only when used for the "purpose of exploring, developing or producing resources" from the Outer Continental Shelf. 40 CFR 55.2. Neither the FSRU, nor any vessel when calling at the FSRU, will be engaged in any OCS activity. Had Congress intended the expanded provisions of section 328 to apply to deepwater ports, Congress had the power and opportunity to include deepwater ports within the scope of facilities covered by section 328. It did not do so. Thus, the section 328 OCS air rules cannot properly be treated as "applicable provisions" of the CAA with which a deepwater port must be found in conformity pursuant to DPA § 1503, and EPA lacks the authority to

impose these requirements on Cabrillo Port. See, e.g., *Santa Barbara County APCD v. USEPA*, (D.C. Cir., 1984), *supra*, 32 F.3d at 1181, and *concurring opinion* at 1184 ("[EPA] cannot adopt an amalgam of reasonable but conflicting interpretations, nor can it simply ignore its statutory mandate in favor of what it considers a more rationale policy.") [5]

D. Aside from the DPA's Expressed Vessel Exclusion and the Inapplicability of the OCS Air Rules, EPA Has No Permit Authority Over Such Marine Vessels, and the Agency is Precluded From Attributing Marine Vessel Transit or Hotelling Emissions to the FSRU.

Although not squarely raised in EPA's April 5 preliminary conclusions, we believe it is important to address the subject of marine vessel emissions, since marine vessels will play an essential role in the project, and regulatory determinations on the subject can be expected. The marine vessels expected to call at the FSRU fall into three general categories: i) LNG cargo carriers, ii) assist tugs, and iii) crew and supply boats. Each is to be propelled by internal combustion engines.

EPA's preconstruction and operating permit programs are in general confined to "stationary sources" of emissions; i.e. these programs do not embrace "mobile sources." The CAA defines "stationary source" so as to exclude internal combustion engines used to propel marine vessels such as those that will call at the FSRU. The 1990 CAA Amendments define "stationary source" as follows:

> "Stationary Source". The term "stationary source" means generally any source of an air pollutant except those emissions resulting directly from an internal combustion engine for transportation purposes or from a nonroad engine or nonroad vehicle as defined in section 7550 of this title. 42 USC § 7602(z).

Section 7550 defines "nonroad engine" as an internal combustion engine that is not used in a motor vehicle, among other machinery. 42 USC §7550(10). Accordingly, marine vessels powered by internal combustion engines are not "stationary sources" for

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[5] The improper application of section 328 in this instance would deny BHPB due process of law. See, e.g., *US v. Ame. Nat. Can Co.*, 2000 WL 1060828 at 8 (Aug. 2, 2000, N.D. Ill.) ("The regulated public must be informed in advance of the rules of the game . . . . EPA cannot escape the structures of the notice-and-comment process by cloaking a substantive addition [to a regulation] in the guise of a mere interpretation of an extant regulation.")

purposes of permitting under the CAA. Thus, it is evident that the vessels themselves are not subject to EPA's preconstruction review and operating permit programs.

The CAA also precludes EPA involvement in indirect source review. For example, the Act prevents the attribution of marine vessel emissions to a facility, such as the FSRU, at which such vessels will call. Section 110 of the CAA provides that "no plan promulgated by the Administrator shall include any indirect source review program for any air quality control region or portion thereof." 42 USC 7410(a)(5)(A)(ii). EPA determined in 1982 that marine vessels are "mobile sources" within the meaning of the statute. The D.C. Circuit Court upheld EPA's interpretation, ruling that EPA cannot require consideration of the transit emissions from marine vessels when issuing permits for associated onshore facilities. *Natural Resources Defense Council v. USEPA*, (D.C. Cir., 1984) 725 F.2d 761, 768-771. The court held that considerations related to motor vehicles, which influenced Congress to enact the prohibition against indirect source review in the first place, apply equally to marine vessels. The effect of the court's decision is that marine vessel transit emissions are not subject to mandatory regulation through indirect source review under the CAA.[6]

Thus, a marine vessel's "to-and-fro" emissions must be treated as part of the vessel's normal seagoing activities and not part of the industrial operations at the deepwater port. Under the same rationale, "hotelling" emissions are excluded as well. As a matter of federal law, these vessel emissions should therefore not be considered for Title I or Title V purposes under the DPA.

E. Inconsistent Ventura County APCD Rules on the Subject do not Apply.

EPA supports its preliminary conclusion that Ventura APCD offset rules should apply to Cabrillo Port by referring to the fact that the DPA permits the application of some state law to deepwater ports. The correct application of the statute and decisional law do not support this conclusion. The DPA provides as follows:

> The law of the nearest adjacent coastal State, now in effect or hereafter adopted, amended, or repealed, is declared to be the law of the United States, and shall apply to **any deepwater port** licensed pursuant to this

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[6] The *NRDC* court held that, "[I]t is entirely implausible that a vessel's 'to-and-fro' emissions could be attributable to a marine terminal owner under any approach that the statute would tolerate . . . ," and therefore affirmed the portion of EPA's 1982 regulatory repeal action which categorically excluded "to-and-fro" vessel emissions from the definition of stationary source. *Id.* 725 F.2d at 764

> Act, **to the extent applicable and not inconsistent with any provision or regulation under this Act or other Federal laws and regulations now in effect** or hereafter adopted, amended, or repealed. All such applicable laws shall be administered and enforced by the appropriate officers and courts of the United States. For purposes of this subsection, the nearest adjacent coastal State shall be that State whose seaward boundaries, if extended beyond 3 miles, would encompass the site of the deepwater port. 33 USCS § 1518(b); emphasis added.

Thus, with respect to a "deepwater port" (which, by definition, excludes vessels), the laws of an adjacent coastal state may apply only if not inconsistent with federal law or regulation. The portion of the DPA pertaining to the application of state law underlined above is identical to that used in the corresponding provision of the OCSLA. *See* 43 USC § 1333(a)(2)(A).

The United States Supreme Court explained the effect of this provision in *Rodrigue v. Aetna Cas. & Sur. Co.* (1969) 395 U.S. 352, 355 [89 S.Ct. 1835, 1837]. The Court explained that the provision that some state law is to be incorporated into the federal law was designed to ensure that certain matters subject to traditional state jurisdiction, such as tort claims for injuries to offshore platform oil workers, would not be inadvertently abolished by the OCSLA. Thus, according to our Nation's highest court, only where there is **no federal law** applicable to a particular subject matter may consistent state law be applied. Even in those instances, state law does not exist as state law, but is instead transformed or "federalized" into federal law. As the *Rodrigue* Court explained in discussing the legislative history of the OCSLA, state law was intended only to fill federal voids, when "Federal statutes or regulations of the Secretary of the Interior are inapplicable." *Id.* at 357-58, 23 L. Ed. 2d at 365, 89 S.Ct. at 1838 (*quoting* S.Rep. No. 411 of the Committee on Interior and Insular Affairs, 83d Cong., 1st Sess., 11 (1953).

EPA's April 5 letter makes reference to a portion of the legislative history of the DPA. However, it is apparent from the plain language that Congress actually wrote into the DPA that Congress did not intend state law or regulations, such as the Ventura County APCD permitting rules, to apply where existing federal law or regulations on the same subject exist.

When Congress enacted the DPA in 1974, Congress knew of this identical provision in the OCSLA and how the Supreme Court had interpreted it in the *Rodrigue* case. In choosing to adopt a mirror image of this language in the DPA, it is evident that Congress intended the same types of limitations on the applicability of state law to apply

to deepwater ports as to OCS facilities. Consequently, if existing federal law or regulation covers a particular subject matter, no state law with respect thereto applies.

As explained above, the DPA expressly excludes marine vessels from the subject matter of deep water port licensing requirements. Moreover, Congress has expressly provided in the DPA that U.S. and foreign flag vessels calling at or associated with a deepwater port are subject to "federal jurisdiction" in 33 USC § 1518(c). The CAA expressly excludes such mobile sources from EPA's air permitting programs, and federal law precludes the attribution of vessel transit and hotelling emissions to the deep water port at which the vessels call. These principles of federal law therefore preclude applicability of any state law on these subjects, in particular Ventura County APCD Rule 26.

F. Even if Ventura County APCD Rule 26 Were to Apply, There Could be no Attribution of Combustion Emissions from Marine Vessels When Operating Outside District Waters.

As explained above, federal law controls here and precludes the attribution of any transit or hotelling emissions from marine vessels that call at Cabrillo Port. However, even if Ventura County APCD Rule 26 were applied, there could be no attribution of combustion emissions from marine vessels when operating outside District waters.

The marine vessels that will call at Cabrillo Port are not part of the "stationary source" as the term is defined in VCAPCD Rule 26.1. As explained above, the FSRU and the marine vessels expected to call at the facility do not belong to the same two-digit Standard Industrial Classification code, nor are they part of a "common production process" within the meaning of subsection 27 of Rule 26.1. Moreover, marine vessels are expressly exempt from District permit requirements pursuant to Rule 23.D.

Subsection 27 of Rule 26.1 does provide that "[t]he emissions from all marine vessels which load or unload at the source shall be considered as emissions from the stationary source while such vessels are operating in District waters and in California coastal waters adjacent to the District." However, the subsection goes on to limit the attribution of "combustion emissions" to those occurring while the vessel is in "District waters." The only combustion emissions in District waters expected from marine vessels that will load or unload at Cabrillo Port would be those from the assist tug, crew and supply boats when and if traveling to and from a Ventura County dock or mooring

within three miles of the Ventura County coastline.[7] However, as explained above, federal law, which controls here, precludes the attribution of any such vessel transit emissions.

G. No Federal Conformity Determination Is Required.

In its March 31, 2004 letter to the State Lands Commission, the Ventura County APCD suggested that this project "may be subject to the requirements of the federal General Conformity rule . . . ." The letter refers to APCD Rule 220, which incorporates by reference Title 40 of the Code of Federal Regulations, Part 51, subpart W. We disagree that any such conformity determination is required.

The federal regulations make clear that where, as here, the federal action includes a major new stationary source that requires an NSR or PSD permit, no conformity determination is required. 40 CFR § 51.853 provides in relevant part as follows:

> (d) Notwithstanding the other requirements of this subpart, a conformity determination is not required for the following Federal actions (or portion thereof):
>
> (1) The portion of an action that includes major new or modified stationary sources that require a permit under the new source review (NSR) program (section 173 of the Act) or the prevention of significant deterioration (PSD) program (title I, part C of the Act).

The "federal action" here - - permitting under the DPA - - includes PSD permitting of the FSRU, a "major new stationary source". DPA § 1502(9)(D). "Federal Agencies with permit responsibilities such as the EPA and MMS will retain all distinct permit issuance authority." USCG Memorandum, "Environmental Planning Aspects of the Deepwater Port Act" (1 April 2003). Consequently, no such federal conformity determination is required for this project.

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[7] Under federal law, California's territorial boundaries extend only three nautical miles from the coast, and include a three mile band around the islands off the coast, but exclude waters between the islands and the coast. This excludes the central portion of the Santa Barbara/San Pedro Channels where the FSRU is to be positioned. Indeed, a "deepwater port" is by definition "located beyond State seaward boundaries." 33 USC § 1502(9)(A). Federal law boundaries control over any more expansive state territorial boundaries where operation of federal law is at issue, for example where federal and state law conflict. *Tide Water Marine, Inc. v. Bradshaw* (1996) 14 Cal. 4th 557, 654; citing *People v. Weeren* (1980) 26 Cal.3d 643.670.

CONCLUSION

The OCS air rules are not applicable to the deepwater port licensing process. Cabrillo Port's CAA preconstruction and operating review should be pursuant to federal PSD rules, and there should be no attribution of vessel transit or hotelling emissions to Cabrillo Port. Any Ventura County APCD rules to the contrary are inapplicable. Finally, the project is not subject to the federal General Conformity rule.

Thank you for considering these views. We believe that through further discussion BHPB and EPA can reach a proper resolution of these issues. We look forward to the dialogue.

Very truly yours,

HOLLISTER & BRACE

By _____
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February 9, 2006

Michael Scheible
Deputy Executive Officer
California Air Resources Board
1001 I Street
Sacramento, CA 95814

Dear Mike:

This is in regard to ARB's inquiry about the availability of potential Carl Moyer Program (CMP) projects--which were unfunded due to lack of funds--for the possible use of emission mitigations for the BHP Billiton Cabrillo Port LNG project. The SCAQMD would welcome additional funding for emission reduction projects; however we believe that LNG projects should mitigate not only increased ship emissions, but also any emission increases caused by delivering regasified LNG with a gas quality different from what we currently have. As we testified at the recent CPUC hearings, LNG should be limited to a maximum Wobbe Index of 1360. Please note that our willingness to help mitigate the emissions impacts resulting from port operations does not constitute our support of the project if the natural gas quality concerns are not adequately addressed.

The SCAQMD has just completed a review of potential CMP projects, and is recommending nearly $20 million funding for CMP projects that will achieve 793 tons/year of NOx reductions and 24 tons/year of PM reductions. Nevertheless, there are additional worthwhile projects that represent over 900 tons/yr of emission reductions, for which there was no available funding. We would like to work with ARB and the project proponent on potential funding to realize emission reductions, and believe our participation is beneficial as there are specific desirable criteria used in prioritizing the projects, including cost-effectiveness. It would be prudent to follow the procedures previously established under the original solicitation per State Moyer Program Guidelines, as well as the SCAQMD's policy in administrating the Moyer program. We strongly discourage random selection of eligible projects which may not achieve the most cost-effective reductions. We would be more than glad to meet and discuss this issue. Please do not hesitate to contact me or Fred Minassian, at 909-396-2641.

Sincerely,

Chung S. Liu, D.Env.
Deputy Executive Officer
Science & Technology Advancement
909-396-2105

CSL:MK
cc: Bob Fletcher
Dean Simmeroth
Gary Yee